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Schedule C Issues Facing the Tax Professional

National Society of Tax
Professionals

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Sole Proprietorship Operation

Simplest business entity to create

One owner: no agreements required and
files no documents with federal
government

Capital structure not independent from
the owner

No separate federal income tax return
required: **Form 1040-Schedule C**

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Tax Return Filing Requirements

No separate income tax return filed for a sole proprietorship

The “*check-the-box*” regulations provide individual business owners with:

1. Limited liability and
2. Pass through taxation

A *single member* **LLC** files a **Schedule C**

Separate businesses owned by same individual:
file a *separate* **Schedule C's**

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A Separate Schedule C for Each Separate Business

Rev. Rul. 81-90

Prevents disguising losses of one activity
against another activity with gains

Sec. 6011(a) provides that regulations
may prescribe separate reporting in
instructions and forms

Sec. 6662(a) accuracy penalties may be
imposed if intentional disregard or
negligence

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Husband & Wife Businesses

“Qualified Joint Ventures” of married couples not treated as partnerships

Conduct of a “trade or business” where both spouses materially participate

An “*election*” made by both spouses to allocate income, deductions and credits based on respective ownership interest

Separate **Schedule C** for each spouse

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A Separate Schedule S/E

Addresses issues dealing with the “tax gap”

Could increase overall tax liability on
Form 1040

Separate “social security” benefits for
each spouse

Defines “legal ownership interest” in the
business

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Ease of Liquidation or Sale

Transfer of business ownership: an asset
by asset disposition by sole proprietor

Gain or loss recognized on each business
asset both tangible and intangible

Measure difference of FMV of each asset
against adjusted basis on date of
disposition

Subjected to “recapture” rules

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Sec. 280A

Home Office Deduction

Principal place of business test

Used “*exclusively and regularly*” by taxpayer to conduct “*administrative or management activities*” of a trade or business

No other **fixed location** where taxpayer conducts “*substantial*” administrative or management activities of *the* business

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Home Office Deduction

The “function” test of the Soliman decision
not an issue

House Committee Report support

Taxpayer may perform administrative and
management activities at another location
where activity not substantial

Substantial non-administrative and non-
management activity at another location

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Medical Insurance Premiums

Sec. 162(l) provides deductibility:

Page 1 of Form 1040 for Health and Long-term Care (age limitations)

Coverage for taxpayer, spouse and dependents

Months during year when taxpayer is self-employed

Not eligible to participate in a subsidized plan

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Pension Plans Available

Simplified Employee Pensions: SEPs
Keogh and Profit Sharing Plans
Individual **Sec. 401(k)** Plans
SIMPLE Plans

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Hiring of Related Parties

Deductible compensation and benefits
allowable for spouses and children
providing services to or for the
business

Children under age 18 not subjected to
Social Security and Medicare

Reduction of taxpayer's AGI

Reduction of family unit's tax

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Hobby vs. Business & At-Risk Limitations

Sec. 183: no deduction for an activity not engaged in for profit

Deductions to extent of income generated from the particular activity

Burden of proof: **Reg. Sec. 1.183-2(b)**
factors which help in determining trade or business status

At-risk Issues: **Sec. 465(b)(3)(C), 267(b) & 707(b)(1)**